



**DEFENSE CONTRACT AUDIT AGENCY
DEPARTMENT OF DEFENSE
8725 JOHN J. KINGMAN ROAD, SUITE 2135
FORT BELVOIR, VA 22060-6219**

IN REPLY REFER TO

PAS 730.3.B.2.4

June 26, 2014
14-PAS-009(R)

**MEMORANDUM FOR REGIONAL DIRECTORS, DCAA
HEADS OF PRINCIPAL STAFF ELEMENTS, HQ, DCAA**

SUBJECT: Audit Guidance on Reporting Business System Deficiencies

On June 30, 2014, APPS will deliver a new report format and the revised Working Paper "A" and "A-01" for most activity codes. The new report process includes changes to how DCAA will report business system deficiencies. The audit programs (i.e., 11010, 11060, 11090 and 17741) will include audit steps to reflect the reporting changes.

Clarification to Business System Reporting Guidance – Reporting Finding less Severe than Significant Deficiencies/Material Weaknesses

MRD 12-PAS-012, Audit Guidance on Auditing Contractor Business Systems and Contractor Compliance with DFARS 252.242-7006, Accounting System Administration, introduced the concept of auditors identifying instances of noncompliances in the contractor's business system that do not rise to the level of a significant deficiency/material weakness, but warrant the attention of the responsible contractor and Government management officials. The MRD stated that GAGAS requires these types of noncompliances be included in the report. However, Policy did not envision auditors reporting instances of the noncompliances less severe than significant deficiency/material weaknesses separately in an audit report without also reporting significant deficiencies as defined by the DFARS business system criteria (DFARS 252-242.7005). The MRD did not provide specific instructions on how to report noncompliances that are less severe than a significant deficiency/material weakness but warrant the attention of those charged with governance when no significant deficiency/material weakness needs to be reported. Therefore, we will provide reporting instructions for the two types of business system deficiencies below (i.e., significant deficiencies (material weaknesses under GAGAS) as defined by the DFARS business system criteria and deficiencies less severe than a material weakness but warrant the attention of those charged with governance).

Business System Noncompliances That Are Less Severe Than Material Weakness but Warrant Attention of Those Charged with Governance

When auditors identify noncompliances in the contractor's business system that are less severe than a significant deficiency/material weakness but warrant the attention of those charged with governance, the auditor will issue a memorandum to the Administrative Contracting Officer (ACO). Auditors need to develop the finding (i.e., criteria, condition, cause, effect or potential effect) in the work papers and demonstrate how the severity of the finding does not rise to a

SUBJECT: Audit Guidance on Reporting Business System Deficiencies

significant deficiency as defined by the DFARS business system criteria (DFARS 252.242-7005). The memorandum will include a statement of condition and recommendation (SOCAR) and provide the contracting officer with sufficient information to understand the condition and the severity of the deficiency (i.e., a fully-developed audit finding).

Exception – The only exception to reporting these less severe noncompliances in a memorandum to the ACO is where the auditor will be issuing a report that includes other significant deficiencies or with an opinion on the overall system as follows:

- *Deficiencies found in **other than** a Business System Audit* – When auditors identify both a significant deficiency (material weaknesses under GAGAS) as defined by the DFARS business system clause and noncompliances that are less severe than a significant deficiency, the auditor will include the less severe noncompliances in the audit report in a separate Exhibit titled “Deficiencies that Warrant Attention of The Contracting Officer.” All significant deficiencies/material weaknesses will be in an Exhibit titled “DFARS Significant Deficiencies.”
- *Deficiencies found in a Business System Audit* – When auditors are performing a full business system audit and at the completion of the audit, only deficiencies that are less severe than a significant deficiency (material weaknesses under GAGAS) as defined by the DFARS business system clause but warrant the attention on those charged with governance need to be reported, the auditor will issue an audit report with a qualified opinion identifying the less severe deficiencies in an Exhibit titled “Deficiencies that Warrant Attention of The Contracting Officer.”

Further Assistance

FAO personnel should direct questions regarding this memorandum to their regional offices, and regional personnel should direct any questions to Auditing Standards Division at (703) 767-3274 or e-mail at DCAA-PAS@dcaa.mil.

/Signed/
Donald J. McKenzie
Assistant Director
Policy and Plans

DISTRIBUTION: E